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THE ROLE OF THE BANK OF CANADA

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THE ROLE OF THE BANK OF CANADA

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TABLE OF CONTENTS

THE ISSUE

Central Banks have a variety of responsibilities, including formulating monetary policy, regulating and supervising the financial services sector and advising governments. While they are formally independent of governments, they are also subject to varying degrees of political control. However, overt interference in the formulation of policy by Central Banks is unusual. The need to maintain the confidence of national and international financial markets and of the public means that governments, at least in industrialised countries, normally abstain from imposing their policies roughshod on Central Banks.

Traditionally, the policies of the Bank of Canada have been in harmony with those of the federal government and have occasioned little public comment. However, in the recent past, there has been criticism of the Bank's monetary policy which, it has been suggested, has penalized certain parts of the country at the expense of others. This has led for calls for the Bank to be more "responsive" to the needs of particular regions and even for provincial participation in the formulation of Bank policy.

This paper examines the historical background to the establishment of the Bank of Canada as well as its various current roles. It considers the Bank's place in public policy formulation and the history of the relationship between the Bank and the federal government. It surveys some of the demands for greater control of the Bank's activities by federal and provincial governments, a matter that is of particular interest in the context of the current debate about the restructuring of the federal system. Issues relating to the relationship between the Bank and an independent Quebec, and the Bank's recent policy initiatives are also raised.

INTRODUCTION

Central Banks play a major role in financial and economic life.[1] They formulate and implement monetary policy, a responsibility which has to be exercised in the context of the larger sphere of public financial and economic policy.[2] A Central Bank is primarily a "bankers' bank" with responsibility for maintaining a soundly based commercial banking system. Central Banks are also bankers to governments. They advise national governments with which they must cooperate closely and to whose control they are generally subject. According to Montagu Norman, a former Governor of the Bank of England:

> I think it is of the utmost importance that the policy of the Bank and the policy of the Government should at all times be in harmony - in as complete harmony as possible. I look upon the Bank as having the unique right to offer advice and to press such advice even to the point of "nagging"; but always of course subject to the supreme authority of the Government.[3]

The need for Central Banks in democratic countries to be subject to the legislature has been emphasized also by Mr. Paul Volcker, former chairman of the Federal Reserve System. While Central Banks must be substantially autonomous and be insulated from partisan and political pressures, they must not act in isolation since ". . . the powers and responsibilities of a Central Bank intersect with those of the principal political authorities."[4] A Central Bank in a democracy must therefore develop and sustain its basic policies in the context of a broad range of public understanding and acceptability.[5]

It is therefore of the utmost importance that there should be agreement, or at least the absence of disagreement, between the government and the Bank. While the Governor of the Bank of Canada is subject to the authority of the Minister of Finance, their relationship is virtually one of equality because, ultimately, the Governor has the

weapon of resignation which ". . . would produce a shock on the money markets, one that would threaten the government itself."[6] Indeed, in 1961, the so-called Coyne affair, in which public disagreement between the Diefenbaker government and the Governor, James Coyne, who has been described as ". . . the victim of the most squalid political conspiracy in our history -- which is taking in a lot of territory,"[7] and the extraordinary spectacle of the government's attempt to get rid of him, were seen to be major blows to that government.[8]

The Bank of England, the American Federal Reserve System and the German Bundesbank are independent from their governments to varying degrees. The Bank of England works in co-operation with the Treasury but is subject to its dictates. The Federal Reserve System has greater power than the Bank of England.[9] While it is independent of the Treasury, which also has some Central Banking functions, the two institutions work closely together. The Bundesbank is an autonomous institution with responsibility for monetary policy. If there is a conflict between the Bundesbank and the federal government, the former normally prevails. The Bank of Canada is more like the Bank of England in its relationship to the federal government.[10] While it is virtually independent of the government in the conduct of monetary policy, the Minister of Finance has the ultimate responsibility for the direction of monetary policy.

It is probably impossible to determine objectively if the varying degrees of independence and responsibility for monetary policy of Central Banks have an impact on price stability and the control of inflation. On the surface, it might appear that the more independent Central Banks are more successful in keeping the inflation rate under control. The classic case is Germany where the inflation rate has been kept low while in Britain, on the other hand, the inflation rate has been relatively high, during the recent past. However, many other factors and government policy decisions account for the success or failure of price stability and the control of inflation.

BACKGROUND

Under the Constitution Act, 1867, the federal government is responsible for monetary policy. It has exclusive jurisdiction over currency and coinage, banking, the incorporation of banks, the issue of paper money, savings banks, interest and legal tender.[11] Parliament has passed legislation such as the Bank Act and the Bank of Canada Act to implement these responsibilities.[12]

The Finance Act, 1914 had put in place some of the principal functions of a Central Bank and these were consolidated by the Finance Act, 1923.[13] However, this Act was only ". . . a half-way house on the road towards a Central Bank."[14] The explicit establishment of a Bank of Canada was proposed in 1933 by the Royal Commission on Banking and Currency in Canada which had been established, prior to the decennial revision of the Bank Act to inquire, inter alia, into the functions and operations of the banking and currency systems. The Commission was concerned about the absence of a ". . . single banking authority which, while linked by its activities with national finance and commerce, is nevertheless detached by its constitution and the temper of its administration from the ordinary pursuits of commercial banking."[15]

The Commission concluded that the excellence of the Canadian banking system probably concealed the need for an agency to deal with modern financial problems. The unsatisfactory operation of the credit mechanism under the Finance Act also emphasized the need for a Central Bank. Responsibility for the implementation of the Act rested with the Treasury Board which was, in effect, a committee of the Cabinet and therefore a political body.[16] Thus, the rates charged on advances under the Finance Act ". . . were not used as an instrument of credit expansion and contraction, but were mainly varied to meet the exigencies of the Dominion Government's finances."[17]

In concluding that a Central Bank was desirable, the Commission was emphatic that it should be independent. While the Governor and Deputy Governor as well as some of the directors should be appointed by the government, the Commission stressed that there were ". . . pre-eminent advantages to the state in entrusting the special and highly technical functions of a Central Bank to a body not subject to the vicissitudes of political life."[18]

The Commission spelt out the advantages of establishing a Central Bank which would be simultaneously an instrument and a force. As an instrument, it would enable the state ". . . which must necessarily retain ultimate sovereignty in matters affecting the currency . . ." to give effect to national policy. As a force, the Bank would have certain powers which could be used to achieve the aims of national policy, such as maintaining the external value of the currency.[19] The establishment of a Central Bank was expected to have several other advantages. It would replace the existing undeveloped and anomalous system by a more rational and unified system of control over the credit structure. It would provide authoritative financial advice to the Dominion and possibly to the provincial governments. Finally, it would facilitate the maintenance of relations with other Central Banks and, in concert with them, would help to stabilize international economic activity.[20]

THE BANK OF CANADA ACT

The Bank of Canada Act established a privately owned Bank in 1934. When a new government assumed office in 1936, it became the majority shareholder and, in 1938, it nationalized the Bank by buying the remaining privately held shares.

Responsibilities of the Bank

Like most Central Banks, the Bank of Canada is responsible for ensuring the value of money or price stability. It was established ". . . to regulate credit and currency in

the best interests of the economic life of the nation, to control and protect the external value of the national monetary unit and to mitigate by its influence fluctuations in the general level of production, trade, prices and employment, so far as may be possible within the scope of monetary action, and generally to promote the economic and financial welfare of Canada."[21]

The Bank as Agent

The Bank undertakes a number of duties on behalf of the government, including acting as its fiscal agent. It advises the government on, and manages, the national debt. It is responsible for selling government securities and for buying and selling Treasury bills. It manages the foreign exchange reserves and intervenes in the foreign exchange market.[22] The Bank has the sole right to issue notes for circulation.[23]

The Bank as Principal

The Bank acts as principal in a number of areas. While monetary policy is its major responsibility, it also sets interest rate policy. It does not do so in isolation but with the tacit approval of the Ministry of Finance. The Governor and the Minister, as well as senior officials of both institutions, meet frequently to discuss interest rate policy. While both the current Governor and the former Minister, Mr. Wilson, have suggested that the financial markets rather than the Bank or the government decide what the interest rate will be, it is likely that market participants take their direction from signals put out by the Bank.[24] If signals sent by open market operations such as buying and selling Treasury bills do not get a reaction, the Bank has an array of further responses, such as intervening in the overnight market.[25]

The Role of the Bank vis-à-vis the Financial Services Sector

The Bank plays an important role vis-à-vis the financial services sector. In addition to its responsibility for setting the reserve requirements for commercial banks,[26] it is the lender of last resort for deposit-taking institutions, a role that is common to Central Banks.[27] In the latter capacity and because a sound financial sector is required for the successful implementation of monetary policy, the Bank monitors the financial system carefully. However, the Bank of Canada does not regulate or supervise financial institutions. That responsibility is the prerogative of the Office of the Superintendent of Financial Institutions with which the Bank maintains contact.[28] Moreover, the Bank has the legislative authority to require the Superintendent of Financial Institutions to inspect any financial institution for which he might be responsible.[29] Hence, its lack of direct regulatory or supervisory responsibility over deposit-taking institutions has not been of concern to the Bank.[30]

The Bank also maintains close links with the Department of Finance and other agencies responsible for regulating and supervising financial institutions. The Governor sits on the Financial Institutions Supervisory Committee that was established in 1987 to provide for the exchange of views and information about the supervision and prudential regulation of financial institutions. He is, ex officio, on the board of the Canada Deposit Insurance Corporation. The Canadian Payments Association is chaired by an official of the Bank. As fiscal agent for the government, the Bank has been involved in the creation of a book-based clearing and settlement system for debt securities. Internationally, the Bank of Canada cooperates with the Bank for International Settlements to secure a convergence of the national treatment of the definition and standards of capital adequacy for international banks.[31]

Management

The Bank is managed by a Governor, who acts as Chairman of the Board and Chief Executive, a Deputy Governor and twelve directors. The Governor and Deputy Governor are appointed for a period of seven years ". . . during good behaviour."[32] Additional Deputy Governors may be appointed but they do not sit on the Board. Directors are appointed from a wide range of occupations and regions but cannot be connected, as a director, partner, officer or employee, to a bank, a bank to which the Quebec Savings Banks Act applies, a member of the Canadian Payments Association that maintains a deposit with the Bank of Canada, or an investment dealer that acts as a primary distributor of new Government of Canada securities.[33] The Bank employs approximately 2,400 people, of whom about 750 are located in nine regional offices.

RELATIONSHIP BETWEEN THE BANK AND THE FEDERAL GOVERNMENT

The relationship between the Bank and the government is clear. According to the current Governor, ". . . the Bank is . . . part of government; it operates in a well-defined manner within the framework of government and not separately from it."[34] The Bank of Canada Act provides for regular consultations between the Minister of Finance and the Governor on monetary policy and its relation to general policy.[35] Much of the advice provided by the Governor is necessarily tendered in private.[36] The Bank also advises the government when legislative proposals are being developed relating to areas for which the Bank is responsible or in which it might have an interest.[37]

In the aftermath of the so-called Coyne Affair in 1961, the government clarified its relations with the Bank, by reiterating its ultimate authority for monetary policy, in an amendment to the Bank of Canada Act:

> If notwithstanding the consultations provided for in subsection (1), there should emerge a difference of opinion between the Minister and the Bank concerning the monetary policy to be followed, the Minister may, after consultation with the Governor and with the approval of the Governor in Council, give to the Governor a written directive concerning monetary policy, in specific terms and applicable for a specified period, and the Bank shall comply with that directive.[38]

This authority has been accepted by subsequent Ministers of Finance and Governors.

The Issue of the Independence of the Bank of Canada

In 1933, the Royal Commission on Banking and Currency (the Macmillan Commission) emphasized that a Central Bank must not be subject to political interference.[39] The Minister of Finance, Mr. Rhodes, supported this position in 1934 during the debate on the Bank of Canada Bill. He emphasized that the Bank's independence must be protected since ". . . at times the exigencies of public finance might not be wholly in harmony with banking policies that might be considered wise and essential in the public interest."[40] However, he left no doubt that ultimate authority lay with Parliament. While the authority of the Bank would prevail in any disagreement over credit between the government and the Bank,[41] ". . . the authority and power of Parliament is always supreme, and it is none the less supreme because of the fact that Parliament, in its wisdom, may delegate a portion of its authority in this instance, as it has done in numerous instances."[42] In 1936 Mr. Rhodes reiterated the nature of the relationship between the government and the Bank that is now conventionally accepted. "In the long run the Bank in the performance of a vital sovereign function must be responsible to the sovereign will expressed through governments. There cannot be two sovereigns in a single state."[43] He stressed, however, that the calibre of the directors would ensure the confidence of the government in the Bank.[44]

In 1938, when proposing amendments to the Bank of Canada Act, the Minister, Mr. Dunning, reiterated that the independence of the Governor and the Board of Directors did not absolve the government of its ultimate responsibility for monetary policy.[45] The Bank's general policy must be in agreement with that of the government. Otherwise, the government had the right to introduce legislation to secure such agreement.[46]

The supremacy of the government was reiterated by the Minister, Mr. Illsley, in 1941[47] and again in 1951 by Mr. Abbott, who concluded that the government had the right to change the management of the Bank if it were not satisfied with its policies.[48] In 1954 this position was confirmed by the Governor who suggested, however, that a situation in which a Central Bank was given independence but was still subject to the Ministry of Finance was ". . . a sort of mongrel arrangement, and the Central Bank should be either a pure department of government . . . or it should have an independent responsibility."[49]

In 1956, the government reversed its position on the question of responsibility for monetary policy. The Minister, Mr. Harris, suggested that the intention of the Bank of Canada Act ". . . was not only to vest ownership of the Bank . . . but to vest in the officials of the Bank independent authority . . . ."[50] This abdication of government responsibility was reinforced by Mr. St. Laurent, who declared that ". . . the Prime Minister will not undertake to have Parliament or the members of the opposition act as a court of appeal from the decision made by the Governor of the Bank of Canada -- unless and until Parliament amends the Act which now governs the Bank of Canada."[51]

The position of the St. Laurent government was rejected by the opposition critic, Mr. Fleming.[52] However, once he became Minister of Finance, Mr. Fleming retreated from the position conventionally accepted, prior to the St. Laurent government, as well as his own earlier assertion that the government had ultimate responsibility for

monetary policy. In 1959, he told the House of Commons ". . . that in the matter of monetary policy this Parliament has placed the responsibility and indeed the power in the hands of the Bank of Canada. The government does not exercise any sway in the field of monetary policy."[53] Mr. Fleming reiterated this position in 1961 during the debates on the division of powers between the government and the Bank.[54]

The issue of responsibility for the Bank's policy came to a head in the so-called "Coyne affair." The Governor, Mr. Coyne, and the Minister of Finance, Mr. Fleming, disagreed over the Governor's unwillingness to acquiesce in the government's desire to ease monetary policy. The government was also displeased by the Governor's speeches, particularly those that expressed concern over the volume of foreign investment in Canada. The disagreement became public and attracted considerable attention, including a letter from a number of academic economists criticizing the Governor's policies. It resulted in the unusual step by the government of introducing a bill to declare vacant the office of the Governor of the Bank of Canada. Following his appearance before the Senate Banking Committee, after the Commons' Finance Committee refused to call him to explain his position, Mr. Coyne resigned.

In order to clear up any misunderstanding relating to responsibility for monetary policy, the new Governor, Mr. Rasminsky, proposed the establishment of the following principles: (i) that in the ordinary course of events, the Bank is responsible for monetary policy, and (ii) if the government disapproves of the Bank's monetary policy, it has the right and responsibility to instruct the Bank on the policy that it should carry out.[55] He emphasized the government's ultimate responsibility for monetary policy. If the Governor felt that he could not implement the government's policy, it would be his duty to resign. Similar proposals were made by the Royal Commission on Banking and Finance in 1964 which set out in detail steps to be followed by the Minister of Finance in issuing directives to the Governor, and

emphasized the need to establish a framework to facilitate frequent contact between them.[56] These proposals were included in an amendment to the Bank of Canada Act in 1967.[57]

Subsequent Governors have accepted this interpretation of the government's role vis-à-vis the Bank. Mr. Bouey noted that Mr. Rasminsky had ". . . stressed the advantages of arrangements which gave the Central Bank a sufficient measure of independence within government to be held responsible for monetary policy, and also made it clear that the elected representatives of the people have the ultimate responsibility and have a suitable mechanism through which to exercise that responsibility."[58] In February 1987, members of the House of Commons Standing Committee on Finance and Economic Affairs questioned Mr. Crow about the relationship between the Governor and the Minister of Finance. He reiterated his support for Mr. Rasminsky's position ". . . that, in the final analysis, it is up to the government to decide on the monetary policy of the Bank of Canada, and indeed of Canada itself."[59]

The question of the Bank's "independence" has been raised again, following the announcement of specific inflation targets by the Minister of Finance in his 1991-92 budget.[60] It has been suggested that, because the announcement, which relates to a matter within the Bank's competence, was not initiated by the Bank, the independence of the latter has been compromised and that it has been politicized.[61] This position has also been taken by some Members of Parliament.[62] Other commentators have suggested that the Bank has gained the advantage over the Minister because it has succeeded in persuading him to continue to support its policies, despite considerable political pressures to the contrary.[63] The Governor denies these conclusions. He points out that section 14 of the Bank of Canada Act, which provides for consultation between the Governor and the Minister of Finance on monetary matters, facilitates the Bank's actions.[64]

Coordination of Policies between the Bank and Governments

It should be stressed that the Bank does not operate in isolation. The successful implementation of its policies depends on harmonization with the fiscal policies of the federal and provincial governments. Until relatively recently, the federal government had not undertaken the kinds of fiscal policies that were in harmony with the aims of the Bank's policy.[65] Similarly, some of the provincial governments have pursued fiscal policies at odds with the aim of the Bank's policies. Given the agenda of each government in the current federal system, it is virtually impossible to achieve harmonization. In its absence, the Bank has used interest rate policies to achieve its aims.

In an attempt to deal with the dislocation produced by the divorce between monetary policy and fiscal policy at the federal and provincial levels and to secure the implementation of an effective anti-inflation policy, the Economic Council of Canada has called for greater coordination between the monetary and fiscal policies of the federal government and the fiscal policies of the provinces. Fiscal policies designed to restrain economic growth when there are inflationary pressures will assist the Bank in controlling inflation.[66] It has been suggested that Ontario, for instance, might have adopted restrictive budgets rather than expansionary ones in the later 1980s in order to reduce the overheating in the economy.[67] Moreover, inflation targets should be made the operating base for decisions by all levels of governments, by business and by labour.[68] One means of ensuring that inflation targets are met lies in the recent federal budget which sets such targets, a policy that has the advantage of substantiating the policy of price stability and therefore giving it credibility.[69] This policy underpins the Council's recommendation that the Bank's objectives should be defined clearly and should be seen to be workable.[70] The report of the Constitutional Committee of the Quebec Liberal Party (Allaire report) has also called for the coordination of fiscal policies concomitant with the introduction of a common monetary policy that takes regional interests into account.[71] Moreover, the Group

of 22, a group of eminent citizens consisting of academics, businessmen and former politicians and political advisors, has called for mandatory review of the fiscal policies and plans of the provincial governments together with those of the federal governments, to ensure the concurrence of fiscal and monetary policies.[72]

Accountability of the Bank

Given the leverage over the economy that the Bank possesses, there is a growing feeling that it should be made more accountable. However, there is little agreement about the ways in which this might be accomplished or, indeed, the nature of such accountability. The Ontario government has argued that economic federalism is not working and has called for greater regional control over the policies of the Bank and for a reduction of its powers.[73] One commentator has suggested that there is political hostility towards the Bank because it is not ". . . a democratic institution. It was conceived and created at a time when the public and mere politicians were simply not given access to workings of the Central Bank. It co-exists with elected governments and is beyond the reach of citizens."[74] Moreover, it is "crucial" to determine if the Governor, an unelected official, should be deciding the economic fate of the country and if the government's inability to manipulate monetary policy represents a failure of the democratic process. To rectify this situation, ". . . it's time to place the Bank in the Department of Finance directly under the Finance Minister's thumb." Even this recommendation recognizes that overt interference by the Minister of Finance would damage the Canadian dollar in the international financial markets.[75]

In the light of these calls for greater accountability, it has been reported that, as part of its scrutiny of federal-provincial relations, the federal government is considering proposals that would change the way in which the Bank is governed and in which it conducts its business.[76] The mandate of the Bank, set out in the preamble of the Bank of Canada Act, would be made more precise and the independence of the Bank

would be confirmed.[77] The Bank would be made more accountable through a provincial role in overseeing its operations. The Board of Directors would be replaced by a board of governors chosen by the federal government from lists submitted by the provincial government and members would be appointed for fixed terms. This board would have the power to vote on monetary policy.[78] In return, the provinces would set their fiscal policies on the basis of nationally established targets in order to keep inflation under control. The proposed reform has been characterized as probably ". . . the one good thing to emerge from the coming year of national turmoil."[79]

The federal government is not alone in suggesting that the Bank might, perhaps, pay greater attention to regional issues. The Group of 22 has also called for at least three-quarters of the members of the Board of Directors to be nominated by provincial governments.[80] A similar proposal in the Allaire Report stresses the need for "greater democratic legitimacy" in the formulation of Bank policy.[81] It noted that regional representation in the American Federal Reserve System provides an example of the ways in which regional interests can be taken into account in policy formulation.[82] The Quebec Chamber of Commerce calls for a resident executive committee, whose members would be chosen from lists presented by Quebec and other regions, to assume responsibility for the Bank.[83] The C.D. Howe Institute goes further and suggests that, in order to give the Bank's policies greater political legitimacy and therefore acceptability, the members of the Board of Directors should be nominated by provincial governments and they would serve on a full-time basis, thereby playing a greater role in the management of the Bank.[84] Moreover, it has been suggested that regional input in policy formulation might help to defuse separatist feelings in Quebec. Regional concerns might be met also by the appointment in the regions of senior deputy Governors who would establish business advisory councils.[85]

It should be pointed out that the Bank is aware of regional concerns since directors

are already appointed from different regions. In 1964, this practice had been noted by the Porter Report which also proposed the establishment of regional committees. It was hoped that such committees would increase the Bank's knowledge of developments and public reactions in different parts of the economy, would encourage senior Bank officers to travel more frequently to see conditions at first hand in the rest of the country, and might assist in the creation of an informed public opinion on monetary matters.[86]

It should be stressed that the effectiveness of appointments, such as that of deputy Governors outside Ottawa, may be limited The state of modern communications and the extensive economic and financial relationships between the regions means that economic and financial policies cannot be formulated for particular regions without taking into account their overall effect. Nonetheless, such appointments may provide a useful tool for public relations, particularly for explaining the Bank's policies more fully than at present.

It has also been argued that suggesting that the powers and role of the Bank of Canada should be reconsidered because ". . . Canadians seem bent on re-examining all of their institutions . . ."[87] and the implication that the Bank is not accountable, display ignorance of the relationship between the Bank and the Minister of Finance. The Bank is responsible to Parliament through the Minister of Finance. Whether Parliament takes its responsibilities seriously in this regard is another issue. Some commentators argue that the committee hearings conducted by the Senate Standing Committee on Banking, Trade and Commerce and the House of Commons Standing Committee on Finance and Economic Affairs reveal that Members tend to be poorly briefed and are usually concerned with relatively trivial issues.[88] Although Parliament's authority over the Bank is paramount, ". . . when its committees get to question Mr. Crow, they prefer to ask him puffballs about his expenses and his salary rather than to tackle him on monetary dogmatism."[89] The fact that Members display ignorance or adopt a highly partisan attitude when questioning the Governor about the

Bank's policies is little reason to change the Bank's constitution. The mechanism already exists to make the Bank more accountable. Indeed, the new chairman of the Commons Finance Committee has indicated that he will use this mechanism by investigating the ways in which the Bank sets policy and publicizes its decisions as well as the way in which the Board of Directors is constituted.[90] It may be ill-advised to undertake a re-examination of an institution such as a Central Bank because of hostility towards the particular Governor, because of popular or political, and possibly ill-informed, dissatisfaction, and because of the Governor's unwillingness to surrender to such clamour.

On the other hand, it has been suggested that the proposal that the Governor should be made answerable to provincial interests, under a new federal-provincial power-sharing arrangement ". . . would make for a greater amount of controversy and some pretty nutty policies and reinforce the widening gap that already exists between the Bank and its proper constituency, the private sector."[91] Indeed, there have been calls for the Bank to be given greater influence. While it is unlikely that the Bank will be given powers similar to those enjoyed by the Bundesbank, it has still been suggested that ". . . it is time Canadians seriously considered the offsetting powers over economic policy that other federal states such as West Germany and Switzerland have vested in strong Central Banks. Their economic record is proof of its success."[92]

The debate outlined above has taken place in the context of the difficult economic circumstances in which the country finds itself, conditions which are likely to continue if constitutional uncertainty prevails or if the present configuration of Confederation is changed. In such circumstances, the formulation of sound fiscal policy by both the federal and provincial governments will continue to be difficult.[93] In such circumstances, however, it is important for the Central Bank to remain strong.

THE ISSUE OF REGIONAL INTEREST RATES

The formulation and implementation of monetary policy is centralized in most countries and Canada is no exception. However, relatively high interest rates and the current constitutional ferment have led to calls for monetary policy to take into account regional concerns. A number of provinces and commentators have expressed unhappiness about the Bank's interest rate and anti-inflation policies, which they regard as among the principal causes of the current economic slowdown and as barriers to adjustment.[94] The effects of the Bank's interest rate policy, partly a reaction to the overheated economy in southern Ontario, has led to suggestions that a policy that is suitable for some regions might not be suitable for others.[95]

Any attempt to impose different regional interest rate policies is almost certain to have adverse results.[96] The Governor has spelt out some of the choices that the Bank faced. It could have been focused on the region with the most intense demand pressures but did not do so because it conducts national monetary policy from a national perspective and cannot formulate policy based on developments in particular regions. If it had focused its policy on the region with the weakest demand, pressures would have been inflationary for the entire country.[97] Such pressures would have caused minimal interest rates to rise, thus ensuring the loss of the long-run benefits of easy money and incurring the costs of a permanent rise in the inflation rate.[98] The implementation of separate interest rates for the different regions would have also raised many difficult administrative questions. As the Royal Commission on the Economic Union and Development Prospects for Canada (the MacDonald Commission) pointed out, ". . . the mobility of capital within the economic union does not permit interregional variation in interest rates."[99]

Most important, the concept of different regional interest rates challenges the premise that Canada is a common currency area.[100] Moreover, the Bank argues that there can be one monetary authority only.[101] The Governor has stressed that ". . . the

Bank of Canada conducts a national monetary policy, on the basis of national levels of economic activity and inflation. While economic conditions may diverge among regions, decisions about monetary perspective must necessarily be taken from a national perspective."[102] The existence of a unified Canadian financial system, which allows savers and borrowers to benefit from the broadest range of opportunities and from wide competition among financial institutions and instruments, requires uniform interest rates. Indeed, the question of setting regional monetary policies is ". . . hardly relevant since it is not in fact possible. A country with a common currency and well-developed financial markets cannot have in any way levels of interest rates, or rates of monetary expansion, that would be systematically different in different regions or provinces."[103]

Even if the status quo is not considered to be the optimal policy and that there can be some institutional accommodation, it has been acknowledged that ". . . given the weak economic performance of many regional economies, this is a singularly inopportune time to engage in such a change. . . . 'Steady as she goes' appears to be the appropriate policy to pursue for the present."[104]

Since a Central Bank must, by definition, be a national institution and must frame its policies in a national context, calls for regional interest rates might be interpreted as being part of a program for the greater decentralization of federal institutions. The validity of the case for decentralizing a Central Bank seems highly questionable, if the institution, in the sense in which it functions in industrialized countries, is to have any impact.

THE BANK OF CANADA AND QUEBEC

In the current discussion regarding the issue of sovereignty-association or independence for Quebec, the issue of regional interest rates has been linked logically to proposals that the Bank should treat Quebec as a special case.

The Allaire Commission has called for the Bank to take into account regional interests when setting monetary policy but stresses that the Bank should remain independent.[105] Similar calls for the regionalization of the Bank's policy and for the Bank to be more "sensitive" to the needs of the regions have come from Senator Castonguay.[106] The Bélanger-Campeau Commission goes further and, in discussing the possibility of independence, has clarified the policy that an independent Quebec should follow. In order to facilitate economic contact between Quebec and Canada, the Commission recommends that Quebec retain the Canadian dollar and therefore the Bank of Canada, although it recognizes that such a policy would not allow Quebec to exercise autonomy in monetary policy.[107]

The Bélanger-Campeau Commission also recognizes that an independent Quebec will be unable to guarantee a strong currency and the federal government is unlikely to give Quebec partial control of the Bank. This will necessarily constrain Quebec's ability to declare sovereignty or even to enter into a form of sovereignty-association.[108] Courchene has also reiterated that a monetary and economic union between Canada and Quebec under new constitutional arrangements, is likely to be neither politically nor economically feasible.[109] Despite the opinion of the Parti Québecois that Quebec would be able to establish its own Central Bank and currency successfully if the federal government does not agree to share control of the Bank of Canada and the currency,[110] it has been suggested that ". . . an independent Quebec without Bank of Canada backing or the Canadian dollar as the medium of exchange would be made into monetary mincemeat."[111] The population of Quebec is unlikely to accept a massive drop in its standard of living that will almost certainly result if the terms of separation between Canada and Quebec are onerous for Quebec. More to the point, the relative success of the Bank's anti-inflationary policy is likely to be the major factor persuading Quebec of the benefits of continued membership of the Canadian monetary union.[112]

THE BANK'S POLICY OF PRICE STABILITY

During the 1980s growing government debt, widespread expectations that governments should continue to provide services and the public's reluctance to pay higher taxes for such services, have given federal and provincial governments little room for manoeuvre. The Bank has had to control inflation while ensuring, simultaneously, that economic growth is not hindered.[113] It has had to balance short-term political demands with the demands of the marketplace. "Just how the central bank is supposed to accomplish this in the face of the insatiable borrowing demands of government, inflationary wage settlements, and integrated capital markets wherein huge sums move instantly to the source of higher returns making exchange rates exceptionally volatile, is never quite explained."[114]

Since the recession of the early 1980s, the Bank's policy has been designed to achieve price stability. During the second half of the decade, it had been preoccupied with inflation resulting from overheated economic growth and subsequent demand pressures, and since 1987 it has tightened monetary conditions progressively. In January 1988, the Governor pointed out that, given these conditions, it was ". . . more essential than ever to provide policy with a framework that is directed as clearly as possible at ensuring moderate expansion in dollar spending in the Canadian economy."[115] He clarified the Bank's policy. "Monetary policy should be conducted so as to achieve a pace of monetary expansion that promotes stability of money. This means pursuing a policy aimed at achieving and maintaining stable prices."[116] Price stability or the reduction of the inflation rate is therefore the key to a healthy economy. It ". . . is founded on the fact that persistent erosion of the value of money, far from providing any lasting benefits, is bound to mean an economic performance for Canada that falls short of the best Canada can achieve."[117]

The emphasis on price stability is not new. The Royal Commission on Banking and

Finance in 1964 had supported such a policy. In addition to guaranteeing that market dealings would not be undertaken for political reasons unrelated to the broad aims of monetary and financial policy, ". . . the main reason . . . for conferring some measure of autonomy on the Central Bank has been the tendency of governments of all forms to develop the habit of inflating the currency . . . . A special responsibility is imposed on the Central Bank to see that the objective of price stability is not forgotten by government merely because other goals have more political popularity in the short-run."[118]

Undoubtedly, the Bank's policies have not been popular with many other schools of economic thought, including politicians, labour leaders and a number of academics.[119] Fighting inflation is a long-term undertaking and, consequently, is not always a priority for governments or interest groups. Moreover, it has been suggested that the Bank's "tight" monetary policy has inhibited economic activity.[120] According to the Governor, ". . . a number of press commentators and some academic economists seem to find [the notion that general price stability could be a proper central objective for monetary policy to work towards and to maintain] a radical, perhaps even dangerous, notion. It drives them to strong, colourful language."[121]

Despite the protests that have greeted its policies, the Bank has maintained a policy of monetary rectitude and price stability.[122] The Governor has stressed that ". . . the immediate benefits of any action have to be measured against the benefits and costs stretching into the future. This is an awkward fact of life which responsible policy-makers must recognize."[123] In this policy, he has the support of the former chairman of the Federal Reserve System as well as the financial press.[124]

CONCLUSION

The Bank of Canada has a most important responsibility to protect the value of money. Throughout its history, the Bank has carried out this responsibility with considerable success, partly as a result of the independence that it enjoys.[125] The Porter Commission had emphasized that ". . . a status of some freedom also makes more effective the Bank's ultimate safeguard of the public -- the warning stemming from the resignation of its senior management -- since the departure of men of independent standing will usually attract considerable public notice and concern."[126] Inevitably, there have been disagreements between governments and the Bank, although only on one occasion did such disagreement lead to a Governor's resignation. By and large, the Bank has resisted government's proclivities to adopt politically expedient policies although it has not been entirely successful in this regard. Indeed, it has been suggested that by the time Mr. Bouey became Governor, ". . . the Bank's role had become one of bailing out politicians after a dozen years of inflationary excess."[127] The current Governor evidently has the strong support of the government, which has assisted the Bank in the implementation of its monetary policy.[128]

One of the interesting features of the 1980s is the fact that Central Banks have increased their authority. According to the former chairman of the Federal Reserve System, ". . . Central Banks are in exceptionally good repute these days. . . . What we think of as central bankerly qualities, an emphasis on restraint and continuity and prudence, seem to have come more in style."[129] Consequently, they are now regarded as one of the few institutions in any society prepared to impose policies of monetary rectitude. Mr. Volcker suggests that the havoc wrought by the impact of inflation during the 1970s and 1980s in the industrialized world gave central banks the flexibility to deal with inflation through monetary policy.[130] The style and policies of the Bank of Canada seem to have been in unison with those enumerated by Mr. Volcker.

Despite objections, the Bank has repeatedly expressed its desire to continue with its current monetary policy. It is too early to determine if those policies will succeed. However, it is useful to place them in context. Even if some might find it inconvenient or even harmful, the Bank is exercising the rights and responsibilities that have been given to it by statute. In spite of calls for the Bank's powers to be whittled away and for it to be brought under greater political control, all reputable commentators, in Canada and overseas, have stressed the need for Central Banks to retain their autonomy. Any attempt to interfere with the Bank's freedom to frame its policies from a long-term perspective or to require it to consider specific rather than national needs ought also to consider the impact of such a policy on the international markets, given the importance of such markets to the economic and financial well-being of Canada.[131] Moreover, it is probably the only institution that is willing or has the means to impose the kind of policies that are required to confront the financial problems that the country faces.

FOOTNOTES

1. For a general survey of the development of Central Banks, see Charles Goodhart, The Evolution of Central Banks (Cambridge, Massachusetts: The MIT Press, 1988). For a description of the principles of Central Banking, see "The Principles of Central Banking," The New Encyclopaedia Britannica, vol. 14, Macropaedia (Chicago: Encyclopaedia Britannica, Inc., 1985), pp. 607-612.

2. For a description of monetary policy and its place in the formulation of public policy, see Bank of Canada, Annual Report of the Governor to the Minister of Finance and Statement of Accounts for the Year 1990 (Ottawa: The Bank, 1991), pp. 7-8.

3. Quoted in "The Principles of Central Banking," The New Encyclopaedia Britannica, Vol. 14, Macropaedia, p. 609.

4. Paul A. Volcker, "The Triumph of Central Banking?" The 1990 Per Jacobsson Lecture (Washington, D.C., 23 September 1990), p. 18.

5. Ibid.

6. Val Sears, "PM can't buck Bank of Canada," Toronto Star, 28 March 1989. See also Madeleine Drohan, "Setting the bank rate complex deal," Globe and Mail, 3 May 1990.

7. Sears, "PM can't buck Bank of Canada." This quotation, which is attributed to the Winnipeg editor, Grant Dexter, appears in Sears' article.

8. James Coyne, the second Governor of the Bank of Canada, resigned from the Governorship after disagreeing with Donald Fleming, the Minister of Finance. His refusal to agree to an expansionist monetary policy was one of the major reasons for the government's displeasure and for its determination to force him from office. For Fleming's version of the Coyne Affair, see Donald Fleming, So Very Near: The Political Memoirs of the Honourable Donald M. Fleming: The Summit Years, Vol. 2 (Toronto: McClelland and Stewart, 1985), pp. 302-349.

9. In a recent article, the Wall Street Journal suggested that the Chairman of the Federal Reserve System has lost some of his pre-eminence in policy formulation to the members of the policy committee that consists of the seven Governors in Washington, D.C. and five of the 12 District bank presidents. A price has been paid for this democracy. "The new Fed is more cumbersome. The chairman can't rule with Olympian disdain; he must coax rather than command. Forming a consensus isn't always easy and . . . lengthy debates can have serious consequences for the economy." Alan Murray, "The New Fed: Democracy comes to the Central Bank, curbing Chief's Power," Wall Street Journal, 5 April 1991, p. A1. For further discussion of this issue, see "Fed boss reportedly faces palace revolt," Financial Post, 10 April 1991, p. 6;

Peter Cook, "The best Central Bank is debatable," Globe and Mail, 11 April 1991, p. B2; and "Fed fight could work to delay cut in rates," Wall Street Journal, 15 April 1991, p. A1.

10. For a description of the respective areas of authority of the Government and of the Bank, see "Bank of Canada: Management and Accountability," Bank of Canada Review (June 1978): 9-21.

11. Constitution Act, 1867 (U.K.), 30 & 31 Vic., c. 3, ss. 91 (14), (15), (16), (19) and (20).

12. Bank of Canada Act, R.S.C. 1985, c. B-2.

13. Finance Act, 1923, S.C. 1923, c. 48.

14. Gilbert Jackson, "The Report of the Royal Commission on Banking and Commerce," in Addresses delivered before The Canadian Club of Toronto, Vol. XXXI, Season of 1933-34 (Toronto: Warwick Bros. & Rutter, Limited), p. 243.

15. Canada, Royal Commission on Banking and Currency in Canada (Lord Macmillan, Chairman), Report (Ottawa: The King's Printer, 1933), pp. 61-62. (Hereinafter referred to as the Macmillan Report.) Sir Thomas White and Mr. Beaudry Leman dissented from the proposal to establish a Central Bank.

16. Ibid., p. 66. For a description of the role of the Treasury Board, see Milton L. Stokes, The Bank of Canada (Toronto: Macmillan, 1939), pp. 17-22.

17. Royal Commission on Banking and Currency in Canada, Macmillan Report, p. 59.

18. Ibid., p. 66.

19. Ibid., p. 63.

20. Ibid., p. 69.

21. R.S.C. 1985, c. B-2, Preamble.

22. Ibid., s. 18.

23. Ibid., s. 25.

24. Canada, Parliament, House of Commons, Minutes of Proceedings and Evidence of the Standing Committee on Finance, 34th Parliament, 2nd Session (18 March 1991): 158:30; Idem (19 March 1991): 159:7.

25. Drohan, "Setting the bank rate complex deal."

26. R.S.C. 1985, c. B-2, s. 19.

27. For a description of the Bank's role as lender of last resort, see Bank of Canada, The Submission of the Bank of Canada to the Commission of Inquiry on Certain Banking Operations (Ottawa: The Bank, 1986), pp. 1-6.

28. The Governor, Mr. Crow, has pointed out that, while the Bank of Canada is not a regulator or supervisor of financial institutions, unlike many other Central Banks, ". . . we do have a deep interest in the functioning of our financial system, because we implement monetary policy through that system and are lenders of last resort to deposit-taking institutions." See Canada, Parliament, Senate, Proceedings of the Senate Standing Committee on Banking, Trade and Commerce, 34th Parliament, 2nd Session (29 January 1990): 18:6.

29. Finance Institutions and Deposit Insurance System Amendment Act, R.S.C., c. 18, s. 85 (3rd Supplement), 1987. In 1986, the federal government spelt out its proposals regarding the role of the Bank of Canada vis-à-vis the Office of the Superintendent of Financial Institutions. See Canada, Department of Finance, New Directions for the Financial Sector (Ottawa: The Department, 1986), pp. 30-31.

30. Bank of Canada, The Submission of the Bank of Canada to the Commission of Inquiry on Certain Banking Operations, pp. 21-23.

31. "Introductory Statement by John W. Crow, Governor of the Bank of Canada before the Senate Standing Committee on Banking, Trade and Commerce," reprinted in Bank of Canada Review (February 1990): 18.

32. R.S.C. 1985, c. B-2, s. 6 (3)(a).

33. Ibid., s. 10 (1), (2).

34. "The Bank of Canada and its objectives," Speech by the Governor of the Bank of Canada to the Canadian Club of Toronto, 16 April 1987, reprinted in Canadian Speeches (June/July 1987): 8. For a succinct description of the relationship between the Bank of Canada and the government, see Thomas J. Courchene, Money, Inflation, and the Bank of Canada, Vol. 1 (Montreal: C.D. Howe Institute, n.d.), pp. 9-12.

35. R.S.C. 1985, c. B-2, s. 14(1). See also Drohan, "Setting the bank rate complex deal," for a description of the process involving officials of the Bank and the Ministry of Finance regarding the setting of interest rates.

36. "The Bank of Canada and its objectives," p. 8.

37. Senate, Proceedings of the Senate Standing Committee on Banking, Trade and Commerce (29 January 1990): 18:15.

38. R.S.C. 1985, c. B-2, s. 14 (2).

39. Royal Commission on Banking and Currency in Canada, Macmillan Report, pp. 65-66.

40. The Minister spelt out the government's rationale for establishing a privately-owned bank.

> The question of control is important. Broadly stated, the problem in this connection is that of creating an institution which shall be devoted to the public interest but which shall not be subject to the exigencies of politics in the narrower sense of the word. The services of the Bank should obviously be at the disposal of the government, particularly in times of severe crisis and emergency. Clearly, however, the Bank should not be subject to dictation by the government, for at times the exigencies of public finance might not be wholly in harmony with banking policies that might be considered wise and essential in the public interest.

He explained the rationale for the major features of the legislation establishing the Bank:

1. Private ownership renders the Bank more independent and detached from political controversy than would be the case under direct public ownership.

2. Limitation of profits removes dangers inherent in private ownership, but still offers conservative investment for private capital.

3. Limitation of share holdings, broad diffusion of stock ownership, and the provision that none of the shares may be held by chartered banks or by bankers tend to avoid pressure from particular interests.

4. Initial appointment of officers, including directors, by Governor in Council . . . affords guarantee of proper expert and disinterested leadership.

Canada, Parliament, House of Commons, Debates: Official Report, 17th Parliament, 5th Session (22 February 1934): 827-828.

41. Ibid., p. 840.

42. Ibid., p. 841.

43. Canada, Parliament, House of Commons, Debates: Official Report, 18th Parliament, 1st Session (1 June 1936): 3262-3263.

44. Ibid., p. 3263.

45. Canada, Parliament, House of Commons, Debates: Official Report, 18th Parliament, 3rd Session (20 June 1938): 4055.

46. Ibid., pp. 4059-4060.

47. Canada, Parliament, House of Commons, Debates: Official Report, 19th Parliament, 2nd Session (13 June 1941): 3936.

48. Mr. Abbott spelt out the relationship between the government and the Bank:

> Naturally the Governor of the Bank of Canada, the Minister of Finance and his permanent officials operate in very close consultation, and the relationships are very close. The Bank of Canada has certain defined responsibilities which, under the statute creating it, it is obliged to carry out. The government has other responsibilities, and among other things I suppose government policy can invariably affect the value of currency, and to that extent could negative action which the Bank might attempt to take. . . . [T]he relative relationships between the Bank of Canada and the government . . . broadly speaking . . . are parallel responsibilities. The government, of course, if it were not satisfied with the action taken by the Governor and the directors of the Bank of Canada, would have to change the management of the bank. . . . [I]t is fair to assume that the ultimate responsibility must fall upon the government.

Canada, Parliament, House of Commons, Debates: Official Report, 21st Parliament, 4th Session (20 June 1951): 4393.

49. Canada, Parliament, House of Commons, Proceedings of the Standing Committee on Banking and Commerce, 22nd Parliament, 1st Session (18 March 1954): 714.

50. Canada, Parliament, House of Commons, Debates: Official Report, 22nd Parliament, 3rd Session (10 August 1956): 7352.

51. Ibid.

52. Canada, Parliament, House of Commons, Debates: Official Record, 22nd Parliament, 3rd Session (11 August 1956): 7458.

53. Canada, Parliament, House of Commons, Debates: Official Record, 24th Parliament, 2nd Session (27 April 1959): 3098-3099. This position was also accepted by the Bank. In 1956, the Governor informed the House of Commons Standing Committee on Banking and Commerce as follows:

> The only action the management of the Bank can take is that which they themselves believe is the proper action for them to take on their own responsibility.
>
> I do not think that it follows . . . that because the government can bring about the removal of the Governor of the Bank, therefore the Governor of the Bank must do whatever the government wants him to do. Nor does it follow in fact that the government expresses views of a kind that would require action by the Bank contrary to its own views of what should be the appropriate monetary policy at that time. Certainly Parliament is supreme, and the government, having a majority in Parliament, is in a position, if it thinks strongly enough about a matter, to bring about a change in the management of the Bank. I feel that this is a very proper safeguard of the public interest . . . . This safeguard does not relieve the Bank of its responsibility, and it does not alter the fact that normally I think you would expect the Bank to take the initiative in matters which fall properly within its own sphere. The Bank is not in the position of daily receiving instructions - or indeed receiving instructions at all - from the government in those matters which by statute are assigned to the responsibility of the management of the Bank.

Source: Canada, Parliament, House of Commons, Minutes of Proceedings and Evidence of the Standing Committee on Banking and Commerce, 22nd Parliament, 3rd Session (22 May 1956): 373-374.

Three years later, Mr. Coyne reiterated the prevailing wisdom regarding the division of powers. He told the Canadian Club of Montreal that ". . . the best approach was for the Bank of Canada to exercise its responsibility for money supply . . . while the government exercised its responsibility for fiscal policy and public debt policy." See Bank of Canada, "Money and Growth: Remarks by Mr. J.E. Coyne, Governor of the Bank of Canada, prepared for delivery at a meeting of the Canadian Club of Montreal, 16 November 1959," News Release, 16 November 1959, p. 14.

54. Canada, Parliament, House of Commons, Debates: Official Record, 24th Parliament, 4th Session (21 February 1961): 2256-2257. The debate on this issue is instructive. The Leader of the Opposition, Mr. Pearson, spelt out the conventionally accepted division of powers between the government and the Bank while the Minister of Finance abandoned any claim to government control over the Bank.

55. Bank of Canada, "Statement by Louis Rasminsky, Governor of the Bank of Canada," News Release, 31 July 1961, p. 1. The Governor spelt out the ways in which the two principles would work:

> The first principle is designed to ensure that the Bank has the degree of independence and responsibility necessary if it is, in the language of the Bank of Canada Act, " to regulate credit and currency in the best interests of the economic life of the nation." To discharge this duty the Bank must be sufficiently independent and responsible in its operations to be able to withstand day-to-day pressures from any source. But in the longer run, if there should develop a serious and persistent conflict between the views of the government and the views of the Central Bank with regard to monetary policy which, after prolonged and conscientious efforts on both sides, cannot be resolved, the government should be able formally to instruct the Bank what monetary policy it wishes carried out and the Bank should have the duty to comply with these instructions. The exercise of this authority by the government would place on government direct responsibility for the monetary policy to be followed. If this policy, as communicated to the Bank, was one which the Governor felt he could not in good conscience carry out, his duty would be to resign and to make way for someone who took a different view.

56. Canada, Royal Commission on Banking and Finance (The Honourable Dana Harris Porter, Chairman), Report (Ottawa: Queen's Printer, 1964), pp. 542-544. (Hereinafter referred to as the Porter Report.)

57. R.S.C. 1985, c. B-2, s. 14 (2).

58. Gerald K. Bouey, "Monetary Policy - Finding a Place to Stand," The Per Jacobsson Memorial Lecture, Toronto, 5 September 1982, reprinted in Bank of Canada Review (September 1982): 4. Subsequently, the Bank also spelt out succinctly its relationship with the Minister of Finance:

> The Bank of Canada's primary function is formulating and implementing monetary policy. The Bank of Canada operates with a large measure of independence. At the same time, there is regular consultation between the Governor of the Bank of Canada and the Minister of Finance. The fact that the Bank of Canada Act permits the Minister to issue mandatory directives with respect to monetary policy under certain conditions makes it clear that the Government has the ultimate responsibility for monetary policy.

Source: Bank of Canada, The Submission of the Bank of Canada to the Commission of Inquiry on Certain Banking Operations, p. 1.

59. Canada, Parliament, House of Commons, Minutes of Proceedings and Evidence of the Standing Committee on Finance and Economic Affairs, 33rd Parliament, 2nd Session (5 February 1987): 32:14.

60. For details of the inflation targets, see Department of Finance, The Budget (Ottawa: The Department, 1991), pp. 112-114; and Bank of Canada, News Release, 26 February 1991.

61. See for instance Madeleine Drohan, "Who's in charge here?," Globe and Mail, 28 February 1991, p. B1; Terence Corcoran, "Foundation laid for low-inflation era," Globe and Mail, 28 February 1991, p. B10; and Alan Toulin, "Crow now accused of politicizing Bank role," Financial Post, 27 March 1991, p. 11.

62. House of Commons, Minutes of Proceedings and Evidence of the Standing Committee on Finance (18 March 1991): 158:15, 158:38.

63. Drohan, "Who's in charge here?"

64. House of Commons, Minutes of Proceedings and Evidence of the Standing Committee on Finance (18 March 1991): 158:39.

65. The proposal of the federal government, in the 1991-92 budget, to set limits for deficit reduction should assist the Bank in the pursuit of its policies. However, the tendency of some provinces, particularly Ontario, to continue to run deficits is likely to continue to negate the effects of the Bank's policies.

66. Economic Council of Canada, Transitions for the 90s, Twenty-seventh Annual Review (Ottawa: Supply and Services Canada, 1990), pp. 57-58. For similar proposals, see Norman Cameron and Derek Hum, "Regionalizing Interest Rates," Policy Options Politiques 11:6 (juillet/aout 1990): 27; House of Commons, Minutes of Proceedings and Evidence of the Standing Committee on Finance (19 March 1991): 159:23; and Terence Corcoran, "Time for Crow to set inflation targets," Globe and Mail, 29 November 1990, p. B10.

67. Economic Council of Canada, Transitions for the 90s, p. 57.

68. Judith Maxwell, "Fighting inflation with less pain," Financial Post, 5 April 1991, p. 7.

69. Brian Hollohan, "A Five-Cent Nickel: In Pursuit of Price Stability," Canadian Business Review (Spring 1991): 24.

70. Economic Council of Canada, Transitions for the 90s, p. 55.

71. Quebec Liberal Party, Constitutional Committee (Jean Allaire, Chairman), A Quebec Free to Choose (Montreal: The Party, 1991), p. 42.

72. Group of 22, Some Practical Suggestions for Canada (Ottawa: The Group, 1991), p. 21.

73. Derek Ferguson, "Rae wants limits on central bank," Toronto Star, 24 October 1990.

74. Toulin, "Crow now accused of politicizing Bank role."

75. Philip DeMont, "Time to Trim Crow's Wings," Policy Options (July/August 1990): 14.

76. Giles Gherson, "A reformed Central Bank ties Premiers," Financial Times of Canada, 8-14 April 1991, p. 4. There has been no official confirmation of these proposals.

77. Ibid. Once its mandate has been made more precise and its independence guaranteed, the manner in which the Bank is governed should not be a cause for concern. The federal government would have veto powers over the appointment of the individuals nominated by the provinces which would ensure that unsuitable candidates would not be appointed.

78. This proposal is similar to the proposals in the Meech Lake Constitutional Accord which sought to give the provinces the right to submit lists of nominees for appointment to the Senate and the Supreme Court.

79. Gherson, "A reformed Central Bank ties Premiers."

80. Group of 22, Some Practical Suggestions for Canada, p. 20.

81. Constitutional Committee, A Quebec Free to Choose, p. 30.

82. Ibid., p. 42. The present Board consists of directors from all parts of the country and regional representation is one of the factors taken into consideration when such appointments are being made.

83. Quebec Chamber of Commerce, "Quebec's Political and Constitutional Future: Its Economic Dimension," Presentation to the Commission on the Constitutional and Political Future of Quebec (Michel Bélanger and Jean Campeau, Co-chairmen) Quebec City, 7 November 1990, p. 29.

84. David E.W. Laidler, How Shall We Govern the Governor? (Toronto: C.D. Howe Institute, 1991), pp. 21-27. For an interesting proposal for giving greater legitimacy to Central Banks and thus ensuring greater acceptability of their policies, see Andrew Coyne, "The Vote Standard," National Review, 10 June 1991, pp. 23-29.

85. Madeleine Drohan and Barrie McKenna, "Decentralizing the Central Bank," Globe and Mail, 25 March 1991, p. B1.

86. Royal Commission on Banking and Finance, Porter Report, p. 549.

87. Toulin, "Crow now accused of politicizing Bank role."

88. For a devastating account of the lack of preparedness of Members and the superficiality of their questions to the Governor of the Bank when he appears before the House of Commons Standing Committee on Finance and Economic Affairs and the contrast with the preparedness of the House and Senate Banking Committees in the American Congress, see Giles Gherson, "Ottawa's mindless grilling of Crow," Financial Times of Canada, 25 March 1991, p. 4.

89. Peter Cook, "The best Central Bank is debatable," Globe and Mail, 11 April 1991, p. B2.

90. Alan Toulin, "MPs to probe Bank of Canada," Financial Post, 4 June 1991, p. 6.

91. Cook, "The best Central Bank is debatable."

92. Peter Cook, "The model for a strong central bank in the post-Meech era," Globe and Mail, 4 June 1990, p. B2. For a discussion of the policy of the German Bundesbank, see Edward Greenspan, "Polemics," Report on Business Magazine (March 1991): 19-20.

93. "The model for a strong central bank in the post-Meech era." See also Terence Corcoran, "Bank of Canada needs in-depth look," Globe and Mail, 8 January 1991, p. B12, for a discussion of ways in which the Bank might be reformed.

94. The Economic Council of Canada suggests that "Anti-inflation policies that impose a heavy burden on many regions and sectors of the economy can seriously impede the adjustments in employment and investment that will be necessary during the 1990s." Economic Council of Canada, Transitions for the 90s, p. 49.

95. It has been suggested that ". . . Ottawa's money monopoly is a particularly acute problem for Canada because the country is not an optimal currency area. The Bank of Canada must pursue a policy based on aggregates in a country that is sectionally diverse and economically dominated by Ontario and Quebec. The result is that some region is suffering inappropriate monetary policy almost all the time." See Peter Brimelow, "Decentralize Ottawa's control of money supply," Financial Post, 21 August 1990, p. 11. For a more detailed survey, see Canada, Royal Commission on the Economic Union and Development Prospects for Canada, Economic Management and the Division of Powers (Ottawa: Supply and Services, 1986), pp. 52-54.

96. "Remarks by John W. Crow, Governor of the Bank of Canada to the Edmonton Chamber of Commerce, Edmonton, 27 June 1989," reprinted in Bank of Canada Review (July 1989): 22-23. The Governor reiterated his position to the Standing Senate Committee on Banking, Trade and Commerce on 29 January 1990 when he stressed that ". . . in terms of broad monetary policy there has to be one monetary policy for the country; there cannot be several, because we are one financial market. Monetary policy is concerned with monetary expansion, the pace of expansion of credit and demand in the Canadian economy. That is the level at which we operate and at which we have to operate." See Proceedings of the Standing Senate Committee on Banking, Trade and Commerce (29 January 1990): 18:19.

97. "Remarks by John W. Crow, Governor of the Bank of Canada to the Edmonton Chamber of Commerce, Edmonton, 27 June 1989," pp. 22-23.

98. R.F. Lucas, "The Bank of Canada and Zero Inflation: A New Cross of Gold?," Canadian Public Policy XV:1 (1989): 91.

99. Canada, Royal Commission on the Economic Union and Development Prospects for Canada (Donald S. MacDonald, Chairman), Report, Vol. III (Ottawa: Supply and Services Canada, 1985), p. 161.

100. For a discussion of this issue, see "Regionalizing Interest Rates," p. 27; and Economic Management and the Division of Powers, pp. 52-58.

101. Bank of Canada, Monetary Policy: A Canadian Perspective. Notes for remarks by John W. Crow, Governor of the Bank of Canada to the Chamber of Commerce France-Canada, Paris, 13 November 1990 (Ottawa: The Bank, 1990), p. 3. See also Economic Management and the Division of Powers, p. 58.

102. "Remarks by John W. Crow, Governor of the Bank of Canada to the Edmonton Chamber of Commerce, 27 June 1989," p. 22.

103. Bank of Canada, Monetary Policy: A Canadian Perspective. Notes for remarks by John W. Crow, Governor of the Bank of Canada to the Chamber of Commerce France-Canada, Paris, 13 November 1990, p. 3.

104. Lucas, "The Bank of Canada and Zero Inflation: A New Cross of Gold?," p. 92.

105. Constitutional Committee, A Quebec Free to Choose, p. 30.

106. Senator Claude Castonguay, "Can Canada Find its Way?" Speech to the Canadian Club, Toronto, 18 February 1991, p. 11.

107.Quebéc, Assemblée nationale, Report of the Commission on the Political and Constitutional Future of Quebec (Quebec: The Commission, 1991), p. 58.

108. Arnold Steinberg, "Talk currency with new Quebec," Financial Post, 19 February 1991, p. 14.

109. Thomas J. Courchene, In Praise of Renewed Federalism (Toronto: C.D. Howe Institute, 1991), p. 55. For a detailed treatment of this issue, see Ibid., pp. 23-67.

110. Eric Reguly, "Quebec may cash out: PQ," Financial Post, 27 February 1991, p. 3.

111. Diane Francis, "Quebec must pay the price of independence," Maclean's (21 May 1990): 15.

112. David E.W. Laidler, Money After Meech (Toronto : C.D. Howe Institute, 1990), p. 5.

113. A useful summary of some of the costs of not dealing with inflation is provided in Thomas J. Courchene, Money, Inflation and the Bank of Canada, Vol. 2 (Toronto: C.D. Howe Institute, 1981), pp. 292-296.

114. "Central banks can't do it alone," Financial Post, 13 November 1990, p. 12.

115. "The work of Canadian monetary policy", Eric J. Hanson Memorial Lecture delivered by John W. Crow, Governor of the Bank of Canada at the University of Alberta, 18 January 1988, reprinted in the Bank of Canada Review (February 1988): 15.

116. Ibid., p. 4. For a review of the issues relating to price stability, see Jack Selody, The Goal of Price Stability, Technical Report No. 54 (Ottawa: The Bank of Canada, 1990).

117. "The Bank of Canada and its objectives," p. 6.

118. Royal Commission on Banking and Finance, Porter Report, p. 541.

119. For a discussion of some of the opinions of the economists who have expressed unhappiness with the Bank's policies, see Anthony Hampson, "Economists noisy but wrong to berate Bank," Financial Post, 16 August 1990, p. 1; John McCallum, "Bank of Canada critics still missing the point," Financial Post, 20 September 1990, p. 13; James Rusk, "Eating Crow's strategy," Globe and Mail, 24 July 1990, p. B1; and Mario Seccareccia, Fiscal Deficits and Monetary Policy: Is Governor Crow just another Coyne? (Ottawa: Canadian Centre for Policy Alternatives, 1990).

120. Even some businesses have suggested that the Bank's anti-inflationary policies inhibit their ability to achieve all the benefits that they should under the Canada-US Free Trade Agreement. See John S. McCallum, "Central bank always an easy target for business," Financial Post, 15 November 1990.

121. John W. Crow, "Some Responsibilities and Concerns of the Bank of Canada," Speech delivered by the Governor to the Canadian Economics Association, Windsor, 4 June 1988. Reprinted in the Bank of Canada Review (June 1988): 5.

122. For a discussion of the benefits of price stability, see the Annual Report of the Governor to the Minister of Finance and Statement of Accounts for the Year 1990, pp. 13-15. According to a recent article in the Globe and Mail, Goldman Sachs suggests that the Bank of Canada is determined to continue its tight monetary policy. It characterises the Bank as "North America's Bundesbank" and suggests that "Governor Crow would easily hold down a prominent place on the Frankfurt institution's central council." See Peter Cook, "Spotlighting a radiant financial vision," Globe and Mail, 1 April 1991, p. B2.

123. "The Bank of Canada and its Objectives," p. 6. F.A. Hayek has also summarized the issue well:

> I do not think it is an exaggeration to say that it is wholly impossible for a Central Bank subject to political control, or even exposed to serious pressure, to regulate the quantity of money in a way conducive to a smoothly functioning market order. A good money, like good law, must operate without regard to the effects that decisions of the issuer will have on known groups or individuals. A benevolent dictator might conceivably disregard these effects; no democratic government dependent on a number of special interests can possibly do so. But to use the control of the supply of money as an instrument for achieving particular ends destroys the equilibrating operation of the price mechanism, which is required to maintain the continuing process of ordering the market that gives individuals a good chance of having their expectations fulfilled.

Source: F.A. Hayek, Denationalization of Money (London: Institute of Economic Affairs, 1976), pp. 89-90.

124. Volcker, The Triumph of Central Banking?, pp. 14-15. See also Terence Corcoran, "A Case for Canadian Price Stability," Globe and Mail, 28 November 1990, p. B8; Idem, "Five non-reasons for cheap money," Globe and Mail, 5 December 1990, p. B8; John McCallum, "Hindsight shows us Bank policy was right," Financial Post, 14 March 1991, p. 9; and Idem, "Money We Trust," Business Quarterly 55:3 (Winter 1991): 46-49.

125. Courchene argues that the existing arrangements regarding the division of powers between the government and the Bank are satisfactory. See Economic Management and the Division of Powers, p. 67.

126. Royal Commission on Banking and Finance, Porter Report, p. 542.

127. Peter Cook, "The Bank Governor moves to centre stage," Globe and Mail, 17 April 1989.

128. The cooperation between Mr. Wilson and Mr. Crow seems to have assured the international financial markets that a strict monetary policy would be implemented at virtually any cost. Mr. Mazankowski has apparently said that he will continue to carry out his predecessor's policies. See Giles Gherson, "All the reasons why Maz will stay the monetary-policy course," Financial Times of Canada, 6 May 1991, p. 6.

129. Volcker, The Triumph of Central Banking?, p. 1.

130. Ibid., p. 3.

131. See for instance John S. McCallum, "Let's keep proper view of Bank of Canada's job," Financial Post, 12 April 1990.